BEHIND THE NUMBERS
Quality of Earnings Analysis
February 19, 2021

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Macquarie Infrastructure Corp. (MIC)- Maintain BUY

We are keeping our BUY rating on MIC and not initiating EQ coverage as the company is in the process of selling itself.

Summary

Following 4Q20 results, MIC noted progress on its process to sell the company and return capital to investors. It is worth noting that Signature Aviation was sold for 16x 2019's EBITDA. That business is very similar to MIC's Atlantic Aviation unit, which is now seeing activity return and it continues to invest in future growth for the business. EBITDA pre-COVID was $276 million and finished 2020 at $195 million, but has improved significantly since the travel shut-downs:

Atlantic Aviation EBITDA	4Q	3Q	2Q	1Q
2020	$58	$54	$17	$66
2019	$71	$64	$62	$79

Guidance for Atlantic Aviation is $220-$240 million in EBITDA for 2021 as the business recovers. We think the business should be worth $3.85 billion based on 16x the $240 million figure or $4.4 billion based on 16x the $276 million figure from pre-COVID. Atlantic has expanded operations since 2019 and continues to add hanger space now.

The sum of the parts looks like this:

Sum of the Parts	A.A. at $240	A.A at $276
IMTT sale net of debt	$989.0	$989.0
Atlantic Sale at 16x EBITDA - debt	$2,836.0	$3,412.0
MIC Hawaii at 10x EBITDA - debt - 21% tax	$321.0	$321.0
Total Proceeds	$4,146.0	$4,722.0
Management Fee	$207.0	$289.0
Net to Shareholders	$3,939.0	$4,433.0
Value per share	$45.1	$50.7
less $11 already received from IMTT	$11.0	$11.0
Remaining Value per share	**$34.1**	**$39.7**
Cash on hand after bond tender	$330.0	$330.0
Expected 2021 free cash flow	$130.0	$160.0
Potential extra cash per share	**$5.3**	**$5.6**

- There is a management bonus based on the level of sales proceeds received. The sales proceeds are net of debt, transaction costs, and taxes owed. The bonus requires the sales process be completed in 2021 so much of this could be known before year-end. The bonus is a sliding scale of 2.91%-6.10% of net proceeds.

- Atlantic Aviation has $1.0 billion in debt that would be netted against any sales proceeds and MIC Hawaii the gas utility has $194 million in debt.

- As described below, the goal is to structure a deal that will not incur capital gains taxes on Atlantic Aviation, but would result in taxes on a transfer of MIC Hawaii. We simply assumed 21% of the total net proceeds. The gain is likely smaller than that.

- IMTT was already sold net of its debt. MIC retained cash to retire the corporate level debt and it has now tendered for the bonds. The proceeds net of all debt was about $989 million. Shareholders were paid $11/share or just over $961 million already with $28 million accrued for management bonus.

- Per the CFO on the 4Q20 call this week, MIC has $330 million in cash after paying taxes and fees from the IMTT sale and what will be spent retiring the debt in the tender offer. Also, the company expects to report Free Cash Flow of $130-$160 million from Atlantic Aviation and Mic Hawaii this year. That cash would either reduce the net debt for either business upon sale or would be left over at MIC and distributed to shareholders. This may result in an extra $4-5 per share at the end of this process.

- We estimate MIC's remaining assets being worth $38-$44 per share at this point against the current value of $31 to $32 – above $35, we'd probably not be looking at this as a BUY.

What to watch

- MIC believes that the Hawaiian gas company can be sold, but it will require approval of the public utility commission as well which should require a longer closing period. That is likely going to result in this being the last asset sold. However, if they they sell Atlantic Aviation first, there would be a capital gain tax to pay on the Atlantic sale.

- MIC plans to change its structure to an LLC. The LCC will need shareholder approval and could see a vote in May 2021. However, MIC will delay the actual change to an LLC until they have a deal to sell Atlantic. That will result in a short time of shareholders owning an LLC.

- The Hawaiian gas unit will be migrated up to MIC the LLC – that will be a taxable event. Given the much smaller size, it should be a lower tax bill. That would allow Atlantic to be sold without a capital gains issue and the proceeds distributed to owners of MIC. Selling the remaining LLC that would own MIC Hawaii would be the final step.

- The tender offer for the MIC bonds should be complete within one month, that should also reflect some progress in the necessary unwinding of the full structure.

Explanation of EQ Rating Scale

6- (Exceptionally Strong)- Indicates uncommonly conservative accounting policies to the point that revenue and earnings are essentially understated relative to the company's peers. Higher possibility of reporting positive earnings surprises

5 (Strong)- Indicates the company has no areas of concern with its reported results and we see very little risk of the company disappointing due to recent results being overstated from aggressive reporting in recent periods.

4 (Acceptable)- Indicates the company may have exhibited a minor “red flag”, but the severity of the issue is not yet a concern. Minimal risk of an earnings disappointment resulting from previous earnings or cash flow overstatement

3 (Minor Concern)- Indicates the company has exhibited either a larger number of or more serious warning signs than companies receiving a 4. The likelihood of an immediate earnings or cash flow disappointment is not considered to be high, but the signs mentioned deserve a higher degree of attention in the future.

2 (Weak) Indicates the company’s recently reported results have benefitted materially from aggressive accounting. Follow up work should be performed to determine the nature and extent of the problem. There is a possibility that upcoming results could disappoint as the impact of unsustainable benefits disappears.

1 (Strong Concern)- Indicates that the company’s recent results are significantly overstated and that we view a disappointment in upcoming quarters is highly likely

In addition to the numerical rating, the EQ Review Rating also include either a minus or plus sign. A minus sign indicates that our analysis shows the overall earnings quality of the company has worsened since the last review and there is a possibility the numerical rating will fall should the problem continue into upcoming quarters. Likewise, a positive sign indicates that the overall earnings quality is improving, and the company may see an upgrade in its numerical rating should the trend continue.

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The EQ Review Rating is much more than a blind, quantitative scoring method. While we utilize proprietary adjustments, ratios, and methods developed over decades of earnings quality analysis, the foundation of all of our analysis is reading recent SEC filings, press releases, conference call transcripts and in some cases, conversations with managements.

The EQ Review Rating is not comparable to a traditional buy/sell rating. The Rating is intended to specifically convey the extent to which reported earnings may be over/understated. Fundamental factors such as forecasts for future growth, increasing competition, and valuation are not reflected in the rating. Therefore, a high score does not in itself indicate a company is a buy but rather indicates that recent results are a good indication of the underlying earnings and cash generation capacity of the company. A low score (1-2) will likely result in us performing a more thorough review of fundamental factors to determine if the company warrants a full-blown sell recommendation.

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